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Hearing on Tax Reform and Consumption-Based Tax Systems
Committee on Ways and Means U.S. House of Representatives
July 26, 2011

Mr. Chairman and Members of the Committee,

It is a great pleasure for me to have this opportunity to submit this written testimony to the committee on a very important subject.

In announcing this hearing, Chairman Camp said, "While the Committee thus far has focused on reforming the income tax, tax proposals that would move us away from an income base and instead adopt consumption as the tax base have continued to generate interest as well. Supporters of such approaches believe that taxing consumption rather than income could have important economic benefits, and so as part of our efforts to reform the tax code, the Committee needs to examine those proposals. This hearing will allow the Committee to learn more about two of the most-discussed consumption tax proposals, the FairTax and the VAT."

A reading of the aforementioned paragraph indicates that the Committee's willingness to learn more about consumption tax proposals is based, in no small part, on the prospect of economic benefit. The Committee recognizes that in addition to generating revenue, an important purpose of a tax system is to generate economic benefit. Since eight of the nine individuals who testified in-person at the July 26th hearing mentioned growth, it is reasonable to assume that one of important economic benefits of a tax system should be growth.

Since growth requires increasing rates of productivity and competitiveness, the following Jean Baptiste Say quote is highly relevant to a tax system with an aim of growth: "It is the aim of good government to stimulate production, of bad government to encourage consumption."

Featured in the June 24, 1980 NBC White Paper ***If Japan Can…Why Can't We?,*** was W. Edwards Deming, whose blueprint for transformation was instrumental to the Japanese economic miracle after World War II. The NBC documentary asserted that "America's declining competitiveness and rate of productivity would make the United States' "guns and butter" policies of the past unsustainable and our children will be the first generation of American to have a lower standard of living than their parents". Since this documentary aired over 31 years ago, the prospect of our children being the first generation of American to have a lower standard of living than their parents is not a new concern. Unfortunately, the shock-value this should have had, in 1980, did little to reverse our declining productivity and competitiveness.

More than one of those testifying on July 26th referred to VATs being considered in the United States for more than four decades. This indicates that there has been over four decades of complacency in considering a tax system discouraging consumption and stimulating productivity.

In Chapter 19 of the 1817 classic ***On the Principles of Political Economy, and Taxation***, David Ricardo mentions, in addition to war, the removal of capital and a new tax as destroyers of the comparative advantage which a country before possessed in manufacturing. Ricardo's inclusion of a new tax(s) among his destroyers of competitiveness speaks volumes regarding the increasing numbers of U.S. trading partners enacting consumption taxes over the last 40+ years and the increasing tax rates of these consumption taxes. Especially over the last 20 years, both the number of trading partners with consumptions taxes and increased tax rates assessed on imports have accelerated. A key take-away is that the new tax(s) referred to by David Ricardo do not need to be new U.S. tax(s). New and increasingly higher taxes on U.S. exports being assessed by our trading partners, qualify as new taxes. Unresponsiveness of prior Congresses/Administrations over more than four decades has kept a consumption tax element out of the U.S. Federal Tax System. As David Ricardo, the father of classical political economics warned, ignoring change has subjected U.S. businesses and workers to a similar plight as the frog in the boiling water parable.

The U.S. trade deficit is America's "leak in the dike" stunting our growth. As a result, favorable effects of: the Bush tax-cuts or Obama's stimulus or monetary easing, have been disappointing and sub-prime. A U.S. Consumption tax, alone, is not the silver bullet for closing our trade gap, but it is an important start. Other Ricardian destroyers have reared their ugly heads, over the last two decades, de-coupling comparative advantage from free trade. These destroyers will be the subject of future submissions to the Committee, when hearings on the applicable subject matter take place.

The committee has two options: hold on to the old or embrace the new.

I hope that the following relevant quotes from luminaries, will be helpful to the Committee:

"The U.S. trade deficit is a bigger threat to the domestic economy than either the federal budget deficit or consumer debt and could lead to `political turmoil.' Pretty soon, I think there will be a big adjustment." – Warren Buffett, January, 2006

"It is not the strongest species that survives, or the most intelligent but the most responsive to change" - Charles Darwin

"It is not necessary to change...survival is not mandatory" - W. Edwards Deming

A commonality possessed by Ricardo, Buffett, Darwin and Deming is their ability to be systems thinkers and therefore dots-connectors. The 40+ years of unresponsiveness by prior U.S. Congresses/Administrations must be overcome to restore the United States to its former greatness.

Supplemental sheet listing the name, company, address, telephone and fax numbers of each witness.

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